

AMENDED IN SENATE MARCH 29, 2011

**SENATE BILL**

**No. 395**

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**Introduced by Senators Dutton and Strickland**

February 16, 2011

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An act to add ~~Section 6377 to~~ *and repeal Section 6377 of* the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

SB 395, as amended, Dutton. Sales and use ~~tax~~ *taxes*: exemption: manufacturing and ~~research and development~~ *research*.

The Sales and Use Tax Law imposes a tax on retailers measured by the gross receipts from the sale of tangible personal property sold at retail in this state, or on the storage, use, or other consumption in this state of tangible personal property purchased from a retailer for storage, use, or other consumption in this state, and provides various exemptions from the taxes imposed by that law.

This bill would provide an exemption from those taxes for the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property, as defined, purchased for use by a qualified person, as defined, to be used primarily in any stage of manufacturing, processing, refining, fabricating, or recycling of property, as specified, or to be used primarily in qualified research, as specified, or to be used to maintain, repair, measure, or test that property. The bill would also exempt from those taxes the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property purchased for use by a contractor, as specified, for a qualified person. The bill would require the purchaser to furnish the retailer with an exemption certificate, as specified.

The Bradley-Burns Uniform Local Sales and Use Tax Law authorizes counties and cities to impose local sales and use taxes in conformity with the Sales and Use Tax Law, and existing law authorizes districts, as specified, to impose transactions and use taxes in accordance with the Transactions and Use Tax Law, which conforms to the Sales and Use Tax Law. Exemptions from state sales and use taxes are incorporated into these laws.

This bill would specify that this exemption does not apply to local sales and use taxes, transactions and use taxes, and specified state taxes from which revenues are deposited into the Local Public Safety Fund, the Local Revenue Fund, or the Fiscal Recovery Fund.

*The bill would remain in effect until January 1, 2019.*

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

1 SECTION 1. (a) It is the intent of the Legislature to enact a  
2 competitive tax policy for manufacturers by providing for an  
3 exemption from state sales and use taxes for the sale of, or the  
4 storage, use, or other consumption of, manufacturing equipment  
5 used in the manufacturing process and property purchased for  
6 research.

7 (b) *It is also the intent of the Legislature, in enacting this*  
8 *legislation, to increase the overall economic activity of business*  
9 *in this state. In particular, it is the intent of the Legislature to do*  
10 *all of the following:*

11 (1) *Increase employment for manufacturing, research and*  
12 *development, and associated industries.*

13 (2) *Increase siting for new and expanded manufacturing and*  
14 *research and development facilities in this state.*

15 (3) *Increase capital investment in manufacturing equipment*  
16 *and all other tangible personal property, the sale or use of which*  
17 *is qualified for exemption under this act.*

18 SEC. 2. Section 6377 is added to the Revenue and Taxation  
19 Code, to read:

20 6377. (a) On and after January 1, 2012, there are exempted  
21 from the taxes imposed by this part the gross receipts from the sale

1 of, and the storage, use, or other consumption in this state of, any  
2 of the following:

3 (1) Tangible personal property purchased for use by a qualified  
4 person to be used primarily in any stage of the manufacturing,  
5 processing, refining, fabricating, or recycling of property,  
6 beginning at the point any raw materials are received by the  
7 qualified person and introduced into the process and ending at the  
8 point at which the manufacturing, processing, refining, fabricating,  
9 or recycling has altered property to its completed form, including  
10 packaging, if required.

11 (2) Tangible personal property purchased for use by a qualified  
12 person to be used primarily in qualified research.

13 (3) Tangible personal property purchased for use by a qualified  
14 person to be used primarily to maintain, repair, measure, or test  
15 any property described in paragraph (1) or (2).

16 (4) Tangible personal property purchased for use by a contractor  
17 purchasing that property for use in the performance of a  
18 construction contract for the qualified person who will use the  
19 tangible personal property as an integral part of the manufacturing,  
20 processing, refining, fabricating, or recycling process, or as a  
21 research or storage facility for use in connection with the  
22 manufacturing process.

23 (b) For purposes of this section:

24 (1) “Fabricating” means to make, build, create, produce, or  
25 assemble components or property to work in a new or different  
26 manner.

27 (2) “Manufacturing” means the activity of converting or  
28 conditioning property by changing the form, composition, quality,  
29 or character of the property for ultimate sale at retail or use in the  
30 manufacturing of a product to be ultimately sold at retail.  
31 Manufacturing includes any improvements to tangible personal  
32 property that result in a greater service life or greater functionality  
33 than that of the original property.

34 (3) “Primarily” means tangible personal property used 50 percent  
35 or more of the time in an activity described in subdivision (a).

36 (4) “Process” means the period beginning at the point at which  
37 any raw materials are received by the qualified taxpayer and  
38 introduced into the manufacturing, processing, refining, fabricating,  
39 or recycling activity of the qualified taxpayer and ending at the  
40 point at which the manufacturing, processing, refining, fabricating,

1 or recycling activity of the qualified taxpayer has altered tangible  
2 personal property to its completed form, including packaging, if  
3 required. Raw materials shall be considered to have been  
4 introduced into the process when the raw materials are stored on  
5 the same premises where the qualified taxpayer's manufacturing,  
6 processing, refining, or recycling activity is conducted. Raw  
7 materials that are stored on premises other than where the qualified  
8 taxpayer's manufacturing, processing, refining, fabricating, or  
9 recycling activity is conducted, shall not be considered to have  
10 been introduced into the manufacturing, processing, refining,  
11 fabricating, or recycling process.

12 (5) "Processing" means the physical application of the materials  
13 and labor necessary to modify or change the characteristics of  
14 property.

15 (6) "Qualified person" means either of the following:

16 (A) A person who is engaged in those lines of business described  
17 in Codes 3111 to 3399, inclusive, or 5112 of the North American  
18 Industry Classification System (NAICS) published by the United  
19 States Office of Management and Budget (OMB), 2007 edition.

20 (B) An affiliate of a person qualified pursuant to subparagraph  
21 (A) shall also be considered a qualified person, as long as the  
22 affiliate is included as a member of that person's unitary group for  
23 which a combined report is required to be filed under Article 1  
24 (commencing with Section 25101) of Chapter 17 of Part 11.

25 (7) "Qualified research" means research that meets the  
26 requirements of Section 41(d)(1) of the Internal Revenue Code.

27 (8) "Refining" means the process of converting a natural  
28 resource to an intermediate or finished product.

29 (9) (A) "Tangible personal property," as used in this section,  
30 includes, but is not limited to, all of the following:

31 (i) Machinery and equipment, including component parts and  
32 contrivances such as belts, shafts, moving parts, and operating  
33 structures.

34 (ii) All equipment or devices used or required to operate, control,  
35 regulate, or maintain the machinery, including, without limitation,  
36 computers, data-processing equipment, and computer software,  
37 together with all repair and replacement parts with a useful life of  
38 one or more years therefor, whether purchased separately or in  
39 conjunction with a complete machine and regardless of whether

1 the machine or component parts are assembled by the taxpayer or  
2 another party.

3 (iii) Property used in pollution control that meets standards  
4 established by this state or any local or regional governmental  
5 agency within this state.

6 (iv) Special purpose buildings and foundations used as an  
7 integral part of the manufacturing, processing, refining, or  
8 fabricating process, or that constitute a research or storage facility  
9 used during the manufacturing process. Buildings used solely for  
10 warehousing purposes after completion of the manufacturing  
11 process are not included.

12 ~~(v) Fuels used or consumed in the manufacturing process.~~

13 (B) “Tangible personal property,” for purposes of this section,  
14 shall not include any of the following:

15 (i) Consumables with a normal useful life of less than one year,  
16 except as provided in clause (v) of subparagraph (A).

17 (ii) Furniture, inventory, and equipment used in the extraction  
18 process, or equipment used to store finished products that have  
19 completed the manufacturing process.

20 (iii) Tangible personal property used primarily in administration,  
21 general management, or marketing.

22 (c) An exemption shall not be allowed under this section unless  
23 the purchaser furnishes the retailer with an exemption certificate,  
24 completed in accordance with any instructions or regulations as  
25 the board may prescribe, and the retailer subsequently furnishes  
26 the board with a copy of the exemption certificate. The exemption  
27 certificate shall contain the sales price of the tangible personal  
28 property that the sale of, or the storage, use, or other consumption  
29 of, is exempt pursuant to subdivision (a).

30 (d) (1) Notwithstanding any provision of the Bradley-Burns  
31 Uniform Local Sales and Use Tax Law (Part 1.5 (commencing  
32 with Section 7200)) or the Transactions and Use Tax Law (Part  
33 1.6 (commencing with Section 7251)), the exemption established  
34 by this section shall not apply with respect to any tax levied by a  
35 county, city, or district pursuant to, or in accordance with, either  
36 of those laws.

37 (2) Notwithstanding subdivision (a), the exemption provided  
38 by this section shall not apply with respect to any tax levied  
39 pursuant to Section 6051.2, 6051.5, 6201.2, or 6201.5, or pursuant  
40 to Section 35 of Article XIII of the California Constitution.

(e) (1) Notwithstanding subdivision (a), the exemption provided by this section shall not apply to any sale or storage, use, or other consumption of property that, within one year from the date of purchase, is removed from California, converted from an exempt use under subdivision (a) to some other use not qualifying for the exemption, or used in a manner not qualifying for exemption.

(2) If a purchaser certifies in writing to the seller that the property purchased without payment of the tax will be used in a manner entitling the seller to regard the gross receipts from the sale as exempt from the sales tax, and within one year from the date of purchase, the purchaser removes that property outside California, converts that property for use in a manner not qualifying for the exemption, or uses that property in a manner not qualifying for the exemption, the purchaser shall be liable for payment of sales tax, with applicable interest, as if the purchaser were a retailer making a retail sale of the property at the time the property is so removed, converted, or used, and the sales price of the property to the purchaser shall be deemed the gross receipts from that retail sale.

(f) (1) This section applies to leases of tangible personal property classified as “continuing sales” and “continuing purchases” in accordance with Sections 6006.1 and 6010.1. The exemption established by this section shall apply to the rentals payable pursuant to such a lease, provided the lessee is a qualified person and the property is used in an activity described in subdivision (a).

(2) Rentals that meet the foregoing requirements are eligible for the exemption for a period of six years from the date of commencement of the lease. At the close of the six-year period from the date of commencement of the lease, lease receipts are subject to tax without exemption.

*SEC. 3. This act shall remain in effect only until January 1, 2019, and as of that date is repealed, unless a later enacted statute, that is enacted before January 1, 2019, deletes or extends that date.*

~~SEC. 3.~~

*SEC. 4.* This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.

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